

**Statement of Frank G. Hausmann, Chairman and CEO
CenterSpan Communications Corporation**

**“The Consumer Benefits of Today’s Digital Rights Management
Solutions”**

**House Judiciary Committee
Subcommittee on Courts, the Internet and Intellectual Property**

**Washington, DC
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Executive Summary

- **Software-based intelligent distributed networks, also known in lay terms as “peer-to-peer” (P2P), is both the origin and the future of the Internet. Distributed networks are not inherently infringing or non-secure, as is evidenced by the increasing use of such technology within corporate enterprises to facilitate the sharing of secure content.**
- **CenterSpan is the first company to commercially develop and market a software-based content delivery network supporting the secure and licensed distribution of rich media audio and video entertainment over the Internet.**
- **CenterSpan's C-StarOne™ is a dynamically scaleable, intelligent distributed network capable of supporting low cost storage and delivery of rich media worldwide. It combines cost savings, assurance of content quality and control, and rapid deployment. C-StarOne also provides for accurate information reporting of content distribution that supports market analysis and royalty payment administration.**
- **Existing digital rights management (DRM) technologies such as those used by C-StarOne, provide sufficient security to address the legitimate concerns of copyright owners and are capable of supporting the tremendous market demand for secure digital distribution over the Internet.**
- **DRM technology supports consumer fair use of legitimate content. DRM technology balances consumer fair use expectations with adequate protections for content owners. This balance will assure marketplace success for consumption of digitally distributed rich media.**
- **Legislative proposals to mandate government-selected content security technologies in consumer electronic devices should be rejected in favor of marketplace solutions.**
- **A legislated, affirmative fair use “safe harbor” should be considered by Congress to facilitate the growth and consumer acceptance of digital content distribution services.**

Chairman Coble, Congressman Berman, and other members of the Subcommittee, my name is Frank G. Hausmann. I serve as CEO and Chairman of the Board of CenterSpan Communications Corporation, headquartered in Portland, Oregon. CenterSpan is a NASDAQ-listed (stock symbol: CSCC). CenterSpan develops and markets a dynamically scaleable, intelligent distributed network capable of supporting the low cost storage and delivery of rich media worldwide. My professional background includes extensive computer industry experience in both legal and management roles.

First, I wish to commend the Subcommittee for holding this important inquiry into the digital rights management (DRM) solutions that are available today to create a win-win value proposition for both the providers of copyrighted rich media content and the millions of consumers who wish to access high-quality content on their computers and other electronic devices. The consumer benefits of DRM-protected digitally distributed content include broad access to high quality media at the lowest feasible cost.

Today's hearing will help to further educate both the public and industry about this dynamic sector and the unprecedented opportunity we now have to meet the large, demonstrated consumer demand for digital audio and video delivery. I also wish to compliment Chairman Sensenbrenner, Congressman Conyers, and other Committee members for their continued dedication to this subject, as evidenced by the Committee's recent solicitation of input from industry and the public regarding consensus copyright legislation that could help spur the further development of the online media marketplace.

Technology and the Online Media Marketplace

Mr. Chairman, this Subcommittee is acquainted more than most with the breakneck changes resulting from the worldwide deployment of digital technology, the tremendous challenges it presents to traditional businesses models, as well as to copyright law and policy. You strove to get ahead of the curve with enactment of the Digital Millennium Copyright Act (DMCA) in 1998. And you are actively engaged now in considering whether additional statutory change is needed.

But you also know more than most that the slow and difficult pace of the legislative process lags behind a rapidly evolving digital marketplace. You also understand that, while law and policy can create a supportive framework for a thriving online media marketplace, they cannot create it. That is a job for those who engage in business and technology.

From the point of view of a business person leading a technology enterprise, I can tell you that the tools required to build that marketplace are here today and do not require

additional legislative support. Our company has had a long and in-depth dialogue with all the essential parties comprising that marketplace – the providers of content, online distributors, as well as consumers – and we have a keen understanding of the needs and desires of each member of this new channel:

- Content owners need effective DRM security.
- Distributors need cost-effective storage and delivery technologies.
- Consumers want affordable access to a high-quality interactive media experience.

While there may well be other viable solutions, CenterSpan has developed and can provide a unique suite of content delivery network services that balances the demands, and optimizes the sometimes conflicting objectives, of these key constituencies. Our recent business partnerships with major media companies are clear testimony that “Hollywood” is embracing cutting edge and cost-effective technology as it strives to meet consumer demand. I think we are all aware that there may not be enough time left this year to enact any major amendments to our copyright law. Indeed, Mr. Chairman, it is quite likely that when you return to start the new Congress next January you will see that very significant and positive changes have occurred in the marketplace. This will occur as any residual reluctance to fully engage in online media distribution is swept aside by the realization that effective technological answers to valid concerns are available today and provide significant economic incentives for all members of this new distribution channel.

Company Background and Activities

CenterSpan’s mission is to create the lowest cost, most highly secure digital distribution network -- and we have. By definition, this means that we are committed to the protection of intellectual property (IP). Our proprietary, software-based distributed streaming and downloading technologies are protected by 19 separate patent applications. Our C-StarOne™ service is capable of supporting a variety of DRM technologies that enable content owners to set their own “usage rules” for copyrighted materials.

We have developed and deployed next generation network technology for the low cost delivery of digital rich media and entertainment. Our goal is to develop a secure digital content distribution channel and business model that will provide great economic incentive and benefit to all without policy disagreements and litigation.

In December 2000 we purchased the 4.5 million-customer list and other assets of Scour Exchange at a bankruptcy auction for \$9 million in cash and stock. Scour was a pioneering P2P system for the delivery of audio and video, but its failure to comply with copyright law resulted in a barrage of litigation and subsequent bankruptcy.

In the spring of 2001 we launched the consumer trial of a new legal Scour Exchange, Scour.com, which today is a technology and marketing showcase for our C-StarOne network. Tens of thousands of users are participating in the free trial. C-StarOne supports the secure and licensed distribution of digital content including music, music

videos, broadcast television catalog, full motion video, e-books, documents, as well as digital photos, images and graphics. Our proprietary market research, as well as extensive conversations with all segments of the digital entertainment world, convinces us that there is substantial consumer demand for such digital content services – provided they offer the right value equation which includes ease of use, content, and price.

In February 2001, CenterSpan established a Digital Media and Entertainment Group. The joint executive team of Michael Kassan and Howard Weitzman runs this Los Angeles-based unit. Mr. Kassan formerly served as President and Chief Operating Officer of Western Initiative Media Worldwide, now a division of the Interpublic Group. In 1997, Mr. Kassan was named by Advertising Age as one of the top media executives in the United States. Mr. Weitzman was formerly Executive Vice President of Universal Studios and has been a well-respected entertainment attorney for over 30 years. Both of these accomplished executives came to CenterSpan from Massive Media Group, a developer of DRM based applications and services for the entertainment and advertising markets. Together, they brought to CenterSpan an understanding of DRM technologies, and the entertainment, media, and advertising sectors that is invaluable to our future growth.

Recent Content Distribution Deals

I am proud that CenterSpan's superior technology enabled us to become the first and, so far, only distributed content delivery network to be licensed to distribute copyrighted digital content from major media companies. On February 28th of this year we announced an agreement with Sony Music Entertainment whereby Sony will make recordings available from its catalog of world-famous music performances for CenterSpan to digitally distribute via its secure C-StarOne content delivery network. This non-exclusive agreement marks the first time Sony Music Entertainment has made its artists' music available to a digital distributor for use on a secure distributed content delivery network.

The agreement lets CenterSpan provide music from Sony Music Entertainment artists to a wide variety of online service providers seeking to offer their subscribers streaming and downloadable music. Using C-StarOne, service providers have the flexibility to cost effectively scale their offerings to fit a variety of business models, including pay-per-use, downloadable or streaming content.

At the time of the announcement, Fred Ehrlich, President of New Technology and Business Development at Sony Music Entertainment stated, "Sony Music Entertainment has always supported new technological innovations that help us bring our artists' music to their fans. We are interested in working with peer-to-peer networks that respect copyright, and CenterSpan's C-StarOne network does just that."

The agreement with Sony Music Entertainment is a tremendous validation of C-StarOne as a trustworthy delivery network for a media company's top content. C-StarOne creates a cost-effective distribution channel for worldwide delivery of rich digital media that will enable digital distribution to move from an emerging stage to a growth stage

with solid economics. Our relationship with Sony Music Entertainment is based on a common vision of the future of secure digital distribution. C-StarOne will provide a wide variety of Internet service providers and portals with quick and secure access to top digital media and entertainment content for their Internet subscription or pay-per-use services. This will substantially broaden the availability of digitally distributed music worldwide.

On May 14th, this partnership was taken to a new level when Sony Music Entertainment launched a promotion of songs from five of its artists using Scour.com, CenterSpan's showcase for C-StarOne™, CenterSpan's content delivery network for securely delivering rich media over the Internet. Scour users are able to listen to these Sony Music Entertainment artists' tracks on their computers as many times as they wish for 30 days after downloading. At the time of this announcement, Jim McDermott, Senior Vice President, Operations and Label Relations, Sony Music Entertainment, said, "Sony Music Entertainment has always embraced new technology that furthers our artists' reach, and CenterSpan's C-StarOne One delivery network will allow music fans to share the music that they love with their friends, legitimately. Working with Scour.com gives us great promotional opportunities like this for our artists. This promotion will kick off Sony Music's relationship with CenterSpan on a high note."

On May 21st of this year, Vivendi Universal Net USA (VUNet USA), the U.S. arm of Vivendi Universal's Paris-based Internet and technology unit, announced a letter of intent for VUNet USA to launch a new digital entertainment service using CenterSpan's C-StarOne™ content delivery network. The new service is expected to debut later this year on one of VUNet USA's entertainment properties. In conjunction with the announcement, Steve Sheiner, Chief Revenue Officer of VUNet USA stated, "We look forward to working with CenterSpan to launch an innovative entertainment service that offers premier content to millions of online fans." This new venture will provide a value-added service unique to the media and entertainment market. The suite of value-added services to be utilized includes content aggregation, content hosting and delivery, digital rights management, license clearing, royalty administration and network reporting.

Clearly, these two announcements prove that major content owners and their Washington advocates are recognizing the tremendous potential of legitimate, DRM supported intelligent distributed networks. In remarks delivered on November 6, 2001 before the O'Reilly Peer to Peer Conference here in Washington D.C., Recording Industry Association of America (RIAA) head Hilary Rosen noted:

The problem with peer to peer is not the technology but how it is used. The multiple exciting applications of P to P that are being discussed over these few days show the limitless potential of the technology in multiple ways. The ability to achieve cost savings on storage and bandwidth, the web tools, the meeting applications, the communications applications, the customer service applications are all extremely exciting.

Cost Efficiencies Of Distributed Networks

CenterSpan embraced the software-based content delivery marketplace out of our belief that distributed networks and applications are both the origin and the future of the Internet. The Internet's fundamental support of a widely dispersed and virtually limitless number of participants, coupled with the transmission of digital information through packet switching that breaks up messages and content and sends it between users via multiple routes, was chosen to assure communication regardless of attacks on any single component of the system. The result is the most robust, resilient, and useful communications system in history. Within this fundamental architecture, pushing content to the edge is the best means for providing high quality, on-demand delivery of any content in the most cost-effective manner.

The C-StarOne intelligent distributed network supports compelling bandwidth savings, provides content owners with robust security, and provides subscribers with better speed and reliability. From the user's perspective, the network "looks and feels" like a central server network. But from a content service provider's perspective, content is cut into thousands of "segments" and hosted and distributed from points or "peers" in the network.

All files in the C-StarOne network are encrypted, signed with a digital signature, and encased in a DRM wrapper before being introduced into the system. The content is centrally controlled, indexed and tracked through the network. User machines must be authenticated before content can be downloaded or streamed. This revolutionary network scales easily and naturally because points or "peers" provide additional network redundancy while keeping a tight lid on bandwidth costs. I have no doubt, based on our ongoing business conversations, that content owners and telecommunications providers understand that a software-based, intelligent distributed content delivery network is the only economically viable means of delivering digital content to a large audience.

Applications for Webcasters

The very substantial cost savings that can be achieved through an intelligent distributed network were again documented on April 3rd of this year, when we announced the results of a pilot with RadioCentral to stream Internet radio content using C-StarOne. The results of the initial pilot indicate that RadioCentral realized a more than a 90 percent bandwidth savings over its central server streaming delivery system.

Jim House, Chief Executive Officer at RadioCentral, had this to say: "The relatively high cost of bandwidth has been a barrier for Internet broadcasters and has pushed a number of players out of the market. The critical success factor of this business is centered on growing an audience and getting them to increase their listening time, which correspondingly increases bandwidth costs. CenterSpan's C-StarOne CDN Services reduces bandwidth costs so significantly that it can truly be called an industry-

enabling technology. It is good news for both the provider and the audience because it lowers costs and delivers a better listening experience."

C-StarOne provides the Internet radio industry with an economically compelling alternative for content delivery, allowing it to accommodate a growing audience while keeping a lid on their infrastructure costs. The results of this pilot further validates the security and economics of the C-StarOne distributed network for downloading and streaming rich media. Your Subcommittee has of course been closely monitoring the continuing controversy regarding the recommendations of the CARP regarding the proper royalty rate for the compulsory webcasting license established in the Digital Millennium Copyright Act (DMCA). Regardless of the ultimate disposition of that rate, much of the discussion has neglected to note that a central server-based webcasting model is of very dubious economic viability, given that cost efficiencies do not accrue when larger audience and longer listening time translate into expensive additional requirements for bandwidth. The use of software-based content distribution, as demonstrated by the Radio Central pilot, provides webcasters with a technology that allows their business to grow in a cost-efficient way.

In addition, the integral network reporting function incorporated within C-StarOne provides a means of generating and aggregating content and usage data that must be a part of any royalty payments system. This aspect of our technology works equally well for the compulsory license of non-interactive Webcasting established by the Digital Millennium Copyright Act and for individual content licenses negotiated between copyright owners and Internet distributors.

DRM, Fair Use, and Public Policy

Since enactment of the DMCA, Congress has engaged in a dual enterprise. Your first objective has been to determine the current state and anticipated evolution of digital entertainment technology and applicable law. Today's hearing is a valuable addition to that data gathering process.

Your second task has been to determine whether additional legislative intervention is required to preserve the goals of copyright law and the rights of copyright holders, while promoting the further development of digital distribution of music, movies, and other rich cultural media. Once again, Congress must balance traditional legal values with new technology that, depending on its use or misuse, may promote or undermine the progress of science and the useful arts. CenterSpan believes that what we have already learned in developing the first licensed and secure software-based content delivery network, from Scour's consumer trial, and from our ongoing and precedent-setting joint ventures with major media companies, can be of substantial value to those ongoing Congressional deliberations.

We take strong exception with those who argue that the utilization of DRM is inherently at odds with the fair use rights reserved to individual users of copyrighted material. Depending on whether a consumer is renting or buying digital content, content

owners have a need to establish reasonable time and usage restrictions on digital media in order to have the assurance that Internet distribution will not be the equivalent of commercial suicide. However, the marketplace will penalize excessive DRM restrictions because the digital media distribution business, like the traditional brick and mortar channel, is a consumer service business, and failing to meet the legitimate expectations of consumers will inevitably lead to the failure of digital media ventures.

Although primary reliance should be placed upon market forces, some legislative intervention may be desirable to establish a “middle way” that steers between the conflicting views and agendas of copyright anarchists versus copyright maximalists. This middle way should be firmly grounded in clarifying consumer rights in the digital age. The notion of a new and affirmative basis for assuring the goals of “fair use” was laid forth in the pioneering 2000 National Research Council report, “The Digital Dilemma: Intellectual Property in the Information Age”. After concluding that “fair use and other exceptions to copyright law should continue to play a role in the digital environment”, and that “the fair use doctrine may also prove useful as a flexible mechanism for adapting copyright to the digital environment”, it issued this policy advice:

Recommendation: The committee suggests exploring whether or not the notion of copy is an appropriate foundation for copyright law, and whether a new foundation can be constructed for copyright, based on the goal set forth in the Constitution ("promote the progress of science and the useful arts") and a tactic by which it is achieved, namely, providing incentive to authors and publishers. In this framework, the question would not be whether a copy had been made, but whether a use of a work was consistent with the goal and tactic (i.e., did it contribute to the desired "progress" and was it destructive, when taken alone or aggregated with other similar copies, of an author's incentive?). This concept is similar to fair use but broader in scope, as it requires considering the range of factors by which to measure the impact of the activity on authors, publishers, and others.

CenterSpan believes it may be useful to consider Federal legislation that carves out a digital fair use “safe harbor” to preserve this key protection of informed discussion, criticism, and debate, as well as to affirmatively delineate consumer rights. We have always maintained that the marketplace can best determine the reuse limitations supported by DRM technologies and is most likely to set the optimal balance between the desires of consumers and the legitimate concerns of content owners. However, experience has also led us to conclude that the best means to stabilize the digital media marketplace, reduce disruptive and expensive litigation, and encourage consumers to utilize legitimate services may be the enactment of Federal legislation stating, as clearly as possible, what reasonable and legitimate uses consumers may make of lawfully acquired digital media. Such legislation must recognize and be in harmony with the statutory rights of copyright holders. But it should also be affirmative in nature, going beyond the existing concept of “fair use” which is but a defense to allegations of copyright infringement. Such legislation should be as explicit as possible in laying out how consumers may legally use their copyrighted digital materials. Since it may be

impossible to envision all types of usage supported by future technologies, the legislation should provide clear principles to guide the courts. We are under no illusions that it will be easy to write, much less enact, such legislation. But we do think that it may be the single most important and useful initiative Congress could do to spur the development of licensed online media services.

Conclusion

CenterSpan appreciates this opportunity to share its views, market experience, and vision for DRM-protected content delivery. We look forward to working with the Subcommittee and all others who are striving to assure that the legal and policy structure for digital media in the twenty-first century is fully relevant, and strikes the proper balance between the rights and interests of all stakeholders, in this exciting and rapidly evolving marketplace.

Thank you for letting me share these thoughts with you today. I would be pleased to answer any questions.